



Association of Independent Insolvency Practitioners

By the practitioner, For the practitioner

27 October 2022

Senior Adviser
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Via email: ASICIFMReview@treasury.gov.au

Dear Sir/Madam

Australian Securities and Investments Commission Industry Funding Model Review

We thank Treasury for the opportunity to make a submission on the Discussion Paper regarding the review of the ASIC Industry Funding Model (“**IFM**”). As the IFM has a significant impact on the members of the Association of Independent Insolvency Practitioners (“**AIIP**”), we make the following submissions and comments on behalf of our members and thank the members of the AIIP for providing their thoughts which assisted in preparation of this submission.

The AIIP

The AIIP is an organisation that was established by insolvency practitioners to assist fellow practitioners meet the challenges prevailing in the profession. The AIIP was formed in 2016 and it now has in excess of 190 full professional members. The AIIP recently established another class of associate members where senior members of the profession intend to become registered as a liquidator or trustee in bankruptcy within 5 years. We have approximately 16 associate members at the time of writing this letter. Our members primarily practise in the small to medium enterprise (SME) market and many members are also members of ARITA.

On behalf of AIIP, we now provide the following comments in relation to the ASIC IFM Review, relating to both the features and calculation of the IFM and to the topic of reporting, transparency and consultation. Our comments are limited to our position as Registered Liquidators (“**RLs**”) upon whom the levies are imposed. The other key area addressed in the Treasury Discussion Paper for Fee-for-Service does not directly impact on RLs other than in limited instances, and we therefore have not focused on this area in this submission.

General acknowledgment of the positive aspects of the review

RLs generally are welcoming of any attempts to streamline what is currently a complex, expensive and time-consuming process. We are of the opinion that the IFM currently lacks: -

The AIIP represents more than 200 liquidators and bankruptcy trustees across Australia.

More information about the AIIP can be found at www.aiip.org.au

- Simplicity – the model is not simple to enable simple calculation of the applicable levy,
- Certainty – the calculation of the levies is not provided within sufficient time to allow for certainty for RLs to incorporate the levies into commercial decisions, and
- Proportionality – the levies are not calculated from readily available metrics, and are not based on revenue or other factors, such as asset realisations, which would allow for better equality across RLs practicing in small versus large firms.

A Review of the IFM has been long awaited by RLs (since it commenced) and an outcome which resolves the above failings is welcomed.

In our Association's recent discussions with a Senator, it was admitted that the operation of the ASIC IFM for RLs was mis-understood, and following discussion, the Senator agreed with our Association's position that the levy is not fit-for-purpose as a vehicle to recover costs for RLs, and further, a better and effective regime is available from AFSA who oversee the personal insolvency sector.

1. Industry Funding Model

We note that there are currently seven (7) categories of the IFM. Four (4) are fixed fees, so calculations are relatively simple. A further two (2) categories are based on a percentage of an easily identifiable variable, either market capitalisation or percentage of audit fee, so again the calculations are relatively predictable and simple. Only in the sector where RLs operate is it a mix of flat fee plus overly complicated calculations based on a number of lodgements made by those liquidators. The IFM for RLs is therefore a combination of a fixed fee (currently \$2,500) per liquidator, plus a rate-per-metric, with metrics represented by "notifiable events" being advertisements placed on ASIC's published notices website and lodgements of specific forms with ASIC, as well as the number of administrations entered into that year or continuing from the previous year. The levies also vary where appointments are accepted singularly or jointly with another RL. This adds another level of complexity to the calculation of the overall levy in any given year.

The draft Cost Recovery Implementation Statement ("**CRIS**") is released in June each year with estimates of costs to be recovered at that time. The final CRIS is issued around November of each year, based on the actual costs of ASIC for the financial year just ended. The CRIS then discloses to RLs what the rate for each metric is for that year. That means that RLs are not aware of their likely liability for some months after the relevant dates, perhaps some 15 months after the metrics were incurred.

It has become industry practice for some RLs to charge each external administration for the levies (subject to creditor approval). However, the final CRIS is released at a time that does not enable RLs to accurately charge the external administration for the actual levy. In practice, an estimate is made and approval of that estimate is sought from creditors. The estimates released in June are not confirmed until November.

Some RLs will seek creditor approval for these charges from each external administration, which is a cumbersome process because:

- The RLs don't know the actual cost of specific jobs because the data is not released until (sometimes) 15 months after the event;
- Creditors don't understand the IFM system or how it is calculated and therefore the basis on which the RLs are charging these costs to the external administration (and reducing assets available for distribution to creditors);

- Some RLs seek to charge a “round figure” whereas some RLs try to estimate the cost of the metric and charge a total fee based on the number of estimated metrics in each external administration, causing a lack of uniformity in a system that should otherwise be a simple and transparent calculation for RLs and other stakeholders (such as creditors) to understand; and
- There is no consistency between RLs on how these charges are calculated and approved, so creditors are not sharing these costs proportionately.

RLs are also obliged to check the volume of metrics, to ensure ASIC is charging the correct metrics. This data is not easily extracted from a central database, and if RLs wish to track their metrics at a practice level (i.e., track all lodgements for each of the RLs within one firm), this must be done separately from recording the metric in the individual appointment (so there is a double up in administration time and costs). As such, RLs also bear the cost of confirming their metrics when the annual return and invoice is received from ASIC. For RLs with hundreds of appointments, this can be a time-consuming and costly administrative process.

Smaller practices tend to have high-volume low-cost external administrations, whereas larger practices tend to have low-volume high-cost external administrations. The current IFM results in the smaller practices incurring a greater number of metrics, leading to a higher levy relative to a larger practice. This inequality means that smaller practices (who are usually less profitable) are subsidising the larger practices (who are usually more profitable).

For formal insolvency appointments under the Bankruptcy Act 1966 involving persons and partnerships (not companies), there is a Public Servant or Public Officer that accepts appointments and conducts work that may be without assets to pay for those services. For appointments under the Corporations Act 2001 involving companies (not persons or partnerships) there is no Public Servant or Public Officer that accepts appointments. RLs in private practice are required to perform work without the prospect of payment for their services, for example on companies that have no assets to pay for their time. RLs are often not remunerated for the service they provide to the economy, and will also incur personal out-of-pocket expenses, such as ASIC search fees and the IFM levy for that assetless external administration.

Regardless of the recovery of the levy from the external administration, there is a great deal of unnecessary complexity in the current model.

The AIFP promotes a simpler method of determining the IFM, and our recommendation is for an **asset realisation charge model** similar to the personal insolvency sector. Under this model, AFSA charge a levy by way of a percentage recovered from the realisation of an asset in the bankrupt estate.

This system has been in place for many decades and is well understood and accepted by Registered Trustees (“**RTs**”) and Registered Debt Agreement Administrators (“**RDAAs**”). Historically, the percentage varies (not materially), sometimes annually, subject to the quantum of costs to be recovered. For the last 7 years it has been steady at 7%. The advantages are:

- it is a simple, consistent, and straightforward calculation based on a defined event, being the realisation of an asset;
- creditors can more easily be educated as to the nature and purpose of the levy and how it is calculated and charged;
- it is calculated and paid from the bankrupt estate upon assets being realised rather than waiting for some months until the metric rate is known;

- the RTs and RDAAs are aware of the liability before being appointed to administer the estate, and are not required to make the payment from their own pocket, when the estate has not recovered any remuneration; and
- the reconciliation and the payment of the levy is completed within a few weeks of the end of the financial year, compared to the present model where invoices are issued for payment in March of the following year.

Some types of external administrations such as controllerships, won't have as many metrics, for example, there will be no metric relevant to advertisements for dividends in a controllership appointment. Therefore, RLs who take appointments as receivers and managers will not be charged a levy, even though they are RLs and are regulated by ASIC. The use of an asset realisation charge will see all external administrations, regardless of type or form, be charged a levy based on a percentage of the assets realised, resulting in a more equitable distribution of the IFM amongst all stakeholders.

This method also would result in the percentage being set in advance of the financial year so that RLs know what money needs to be set aside out of the external administration immediately on the realisation of the assets. Any adjustments required as a result of variances would be able to be adjusted in the following year, as with the AFSA model.

We note that there may need to be some changes to legislation to enable the payment of the asset realisation charge as a priority, again similar to the Bankruptcy Act and associated legislation.

Because the levy would be incurred as a cost to the external administration, it will not require the approval of creditors before it is paid out of the external administration. This again will help to keep costs down by avoiding the need to call meetings of creditors or issuing proposals to creditors for such approval. No doubt creditors would also welcome this as they would not be burdened with the unnecessary administrative task of attending to approvals.

The proposed **asset realisation charge model** is fairer because it will be paid on the realisation of an asset, and as a priority i.e., ahead of RLs' remuneration and any other costs of the administration. It will also mean that there is no payment of a levy required to be made by the RLs from personal funds on external administrations that have no recoveries.

The AIIP would be pleased to be involved in any process of mining data in order to assess the likely realisations and asset realisation charge. This data is easily obtainable from the Forms 5602 and 5603 lodged by RLs with ASIC. We are also not aware of the levies currently paid by RLs or other industry participants, in order to compare the current IFM levies with the asset realisation charge model.

2. Reporting, Transparency and Consultation

The AIIP's main concern with reporting is the untimely issuing of the CRIS, whereby currently RLs are not aware of the final metric rate until at least November each year. If RLs directly charge each external administration for the actual IFM, they are not able to do so until invoices are issued in around March the following year, unless they have made an estimate and received creditor approval. Many external administrations could have been finalised before invoices are issued and this leaves the RLs out of pocket.

Because of the way the current model operates, RLs are incentivised to finalise their external administrations as quickly as possible so they are not charged with another metric the following

year. This places RLs under unnecessary pressure to finalise the external administration before 30 June each year (if this is possible given the individual circumstances in each administration).

Our concerns in regard to the transparency of the process include:

- The reporting is inscrutable. The table explaining the detail of how funds are to be spent (estimated at \$4.8 million in 2021-22) in Table 15 of the CRIS issued June 2022 is eleven (11) line items. In our opinion this is too brief, and no further detail is given on what makes up each of these line items. By way of example, the ASIC annual report provides a brief list of the major items undertaken by ASIC in the same period, but the CRIS provides no indication of the cost of those items.
- The reporting each year details that around 47% of costs allocated are for “indirect costs”. Whilst the industry can accept the concept that each industry sector should bear the costs of its regulation, the very high level of “indirect costs” indicates that the industry is charged expenses for ASIC expenses that have nothing to do with the industry sector.
- The estimated costs, even after the end of a period, have been wildly inaccurate. By way of example, the CRIS released in November 2021 estimated that the estimated total levy for the period ended June 2022, being the period ended five months prior, would be \$7.5 million. The CRIS released in June 2022 disclosed that the actual levy for the period ended June 2021 was \$5.1 million. It is inexplicable to our members how an estimate created 5 months after the end of a period can later be disclosed as wrong by 47%. That level of misestimate on what should have been actual levy amounts, gives our members no confidence regarding the amount, nor calculation process of the levy.
- AIIP have been trying since 2015 to determine whether specific costs such as adverse costs orders for unsuccessful actions taken against RLs, are included in the costs to be recovered, and at no time have we been given a direct answer to confirm whether or not they are included. We have not been able to determine from previous reports whether or how such costs are included in any of the line items.
- There is a great deal of inequity between the average IFM levies imposed on RLs and the levy imposed on other comparable sub-sectors. We provide the following calculation based on the CRIS released June 2022

| ASIC Levy - RLs v Auditors - based on CRIS 2021-22 released June 2022 | | | | | |
|------------------------------------------------------------------------------|-----------------------------------|----------------------------|-------------------------------|---------------------------|------------------------|
| Corporate Sector | Estimated Levy for 2020-21 | Actual Levy 2020-21 | Estimated Levy 2021-22 | Number of entities | Levy per Entity |
| Registered liquidators | \$ 7,552,000 | \$ 5,100,000 | \$ 4,778,000 | 668 | \$ 7,153 |
| Registered company auditors | \$ 4,107,000 | \$ 1,800,000 | \$ 985,302 | 3,657 | \$ 269 |

- The most obvious comparison is between RLs and auditors. Calculations from the CRIS released in June 2022 reveal that the average estimated levy per Registered Liquidator is \$7,153 as compared to \$269 for Registered Company Auditors,
- On a gross level the disparity is also evident with the total cost of supervising 668 RLs compared of \$4.8 million against a cost of \$985,000 for 3,657 auditors.
- There is no explanation of why this apparent inequity between RLs and auditors arises. For example, does ASIC provide more assistance or education or information or discipline in the corporate insolvency sector? The reporting does not disclose whether that is the case.

The industry has been actively self-regulating. For example, in two recent examples for financial

loss (Amanda Young and David Leigh), the industry self-regulated and funds were returned immediately by the relevant practices. It is understood that ASIC had a role in disciplinary proceedings after the individual firms had already self-reported the financial loss to ASIC and had also restored the misappropriated funds.

3. Conclusion

We would like to thank Treasury for the opportunity for both face-to-face and written consultation, as for many years we have felt that consultation was lacking. We have had concerns about the IFM levy from the commencement, and as this is a topic of significant importance for all of our members, it is rewarding to be heard and we look forward to a more equitable IFM.

If you have any questions regarding this submission, please do not hesitate to contact us. If there is to be any further consultation with the profession, we would ask that AIIP be invited to participate.

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Yours faithfully

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